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FROM: Louis Lembo/Business Planning

SUBJECT: RJR Nabisco Stock Analyst Presentation

Attached is a copy of a handout distributed at RJR Nabisco's presentation to stock analysts held yesterday at the New York Hyatt. RJR Nabisco executives, CEO Charles M. Harper and CFO Steve Wilson, made the following points concerning the company's financial objectives and Domestic Tobacco performance:

RJR Nabisco's financial situation is stable and the company is committed to improving shareholder value:

- RJRN's primary mission is to produce sustainable earnings growth.
- Management stressed that "cash" net income is a more realistic measurement of the company's true earnings power and will be the company's internal benchmark for the future. Cash net income is defined as net income with amortization of goodwill and trademarks added back. RJRN has $625 million in annual amortization expense. RJRN "cash" net income in 1992 was $1.4 billion versus reported net income of $0.8 billion.
- Management feels that RJRN stock is undervalued relative to other tobacco companies, when it is evaluated using the "cash" approach. RJRN's "cash" P/E ratio is 6.2x vs. 9.3x for PM and 8.0x for American Brands.
- RJRN's objective is to achieve a 20% after-tax "cash" return on equity. Holding to this standard, consolidated business contribution (operating income before amortization, interest and taxes) more than doubles over five years, moving from $2.7 billion in 1993 to $5.5 billion in 1998. RJRN will adopt an aggressive acquisition strategy to help attain this objective.
- "Cash" EPS growth objective is 15% per year. For the nine months ended September 30, 1993, fully diluted "cash" net income per share was down 18% to $.60.
- The capitalization ratio objective is 43% debt. Interest coverage objective is to produce cash flow from operations that is 2.7 times total interest and preferred dividends. Free cash flow will be used to reach the 43% level, then all free cash flow will be reinvested in profit-generating projects. The company's capitalization ratio as of September 30, 1993 was 44% debt.
- The company will not sell any more businesses to reduce debt.
- Acquisitions will be the driving force behind efforts to enhance shareholder value and attain ROE objectives. Management intends to use virtually all its free cash flow of about $500 million annually for this purpose. The acquisition program will focus on international food and tobacco businesses that are government entities or privately held.
- It was indicated that a tax-free spin off of Nabisco "is not in the plan, but plans can change".

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RJR Domestic Tobacco profitability will improve in 1994:

- Mr. Harper stated that the current price war is a short-term event "which could have ended last month, could end next month or two years from now, but it will end as all price wars do."
- Mr. Harper also felt there would be no change in the foreseeable future to the structure of industry pricing. He also commented that price increases could return in "the reasonably near future, given the progress made in closing the price gap and the reduction in cheating (couponing)."
- RJR will emphasize profits over market share in domestic tobacco. The company is willing to accept modest market share losses as the cost of improving earnings.
- Mr. Harper confirmed that RJR Domestic Tobacco earnings will be down approximately $900 million or 42.6% to $1.2 billion in 1993.
- RJR will use the remainder of 1993 to restructure operations and set the stage for 1994.
- Management would not specify how much IFO would grow in 1994 or the dollar amount of fourth quarter 1993 restructuring charges, but reiterated their commitment to income growth in 1994. It is expected that RJR will do their best to pull as many 1994 charges into fourth quarter 1993 as possible.
- RJR will eliminate and reduce costs to reach their goal of increased earnings in 1994.
- RJR will streamline marketing spending and tighten cost and spending control.

Stock analysts reaction to RJR's presentation:

Stock analysts that attended the meeting generally liked what they heard. Jay Nelson of Brown Brothers Harriman reiterated his buy opinion on RJRN. He writes, " We believe that the domestic tobacco industry will be on firmer footing reasonably soon. Also, costs are being cut sharply."

Gary Black of Sanford Bernstein & Co. reiterated his buy rating on RJRN after attending yesterday's meeting. He felt that RJR management was strongly hinting that pricing is likely to resume soon in domestic tobacco. Price increases translate to improved profitability, which translates to a higher stock multiple. He also believes that RJRN will be successful in convincing the market to value the company on "cash" earnings, instead of reported earnings. Mr. Black writes that one potential risk is finding acquisitions that meet the 20% ROE criteria. However, if they do, it will be better for stockholders in the long run than the alternative of using cash flow to retire stock and long term debt.

In regard to RJRN's financial benchmarks, Anton J. Brenner of UBS Securities appeared skeptical that RJR could meet them. He writes, "Since amortization will account for close to half of RJRN's "cash" earnings in 1994, a 15% growth rate would require a 28% increase in net income. Also, because the company is assuming that U.S. tobacco profits do not improve beyond 1994 (they accounted for 49% of income for 9 months and 34% in the 3rd qtr.), this means that International Tobacco and Food profits will have to rise at a 40% annual rate for the company to hit its target. International tobacco profits rose 12.5% for the first nine months of 1993, while Food operating income is increasing at a 10% rate." The difference will need to be derived from acquisitions. "Of course, they would have to offer extremely fast synergy and cost little, and probably require creative deal structures."

Mr. Brenner has a hold rating on RJRN's stock and feels strongly that the company is fairly valued. He states, "It may be that additive acquisitions will allow earnings growth to soar, but we see no reason to pay for unknown acquisitions in unknown businesses at an unknown price up front."

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